Supreme Court, U.S.
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# 85-1190

No. 85-

IN THE

# Supreme Court of the United States

OCTOBER TERM, 1985

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ASSOCIATED GAS DISTRIBUTORS AND
PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,
*Petitioners,*

v.

FEDERAL ENERGY REGULATORY COMMISSION,
*Respondent.*

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## PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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January 15, 1986

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## QUESTION PRESENTED

Whether valuable in-kind consideration may be disregarded by the Federal Energy Regulatory Commission in its enforcement of congressionally-mandated ceiling prices for first sales of natural gas?

## PARTIES TO THE PROCEEDINGS

The parties to the proceedings below included petitioners Associated Gas Distributors * and New York Public Service Commission; respondent Federal Energy Regulatory Commission; Amerada Hess Corporation; Aminoil Inc.; Amoco Production Company; ANR Pipeline Company; Arco Oil and Gas Company; Ashland Exploration, Inc.; Cabot Petroleum Corporation; Chevron U.S.A., Inc.; Cities Service Oil and Gas Corporation; Colorado Interstate Gas Company; Conoco Inc.; Diamond Shamrock Corporation; Elf Aquitaine, Inc.; Exxon Corporation; Getty Oil Company; Gulf Oil Corporation; A.G. Hill; Estate of H.L. Hunt; Hassie Hunt, Inc.; Hunt Industries; Hunt Oil Company; Hunt Petroleum Corporation; Caroline Hunt Schoellkopf; Caroline Hunt Trust Estate; Lamar Hunt; Lamar Hunt Trust Estate; N.B. Hunt; W.H. Hunt; W.H. Hunt Estate; Secure Trusts; Inexco Oil Company; Interstate Natural Gas Association, Inc.; Kerr-McGee Corporation; Marathon Oil Company; Mitchell Energy Corporation; Mobil Oil Corporation; Mobil Producing Texas & New Mexico Inc.; Mobil Oil Exploration & Producing Southeast Inc.; Monsanto Oil Company; Natural Gas Pipeline Company of America; Panhandle Eastern Pipeline Company; Panhandle Trunkline Gas Company; Pennzoil Company; Pennzoil Producing Company; Pennzoil Oil & Gas, Inc.; Pennzoil Louisiana and

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* In accordance with Rule 28.1, the list of parent companies, subsidiaries (except wholly-owned subsidiaries) and affiliates of Associated Gas Distributors is included as an Appendix to this petition.

Texas Offshore, Inc.; Phillips Petroleum Company; Phillips Oil Company; Pinto, Inc.; Placid Oil Company; Sea Robin Pipeline Company; Shell Oil Company; Shell Offshore Inc.; Shell Western E&P Inc.; Sohio Petroleum Company; Southern Natural Gas Company; Sun Exploration and Production Company; Tenneco Oil Company; Tennessee Gas Pipeline Company; Texaco Inc.; Texas Eastern Transmission Corporation; Transwestern Pipeline Company; Texas Production Company; The Superior Oil Company; Transcontinental Gas Pipe Line Corporation; Union Oil Company of California; United Gas Pipe Line Company; and Williams Exploration Company.

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*Petitioners,*

v.

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*Respondent.*

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## PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

---

Associated Gas Distributors ("AGD" or "Petitioners"), an unincorporated association of East Coast gas distribution companies appearing herein jointly and severally, and the Public Service Commission of the State of New York petition for a writ of certiorari to review Section III of the August 19, 1985 decision of the United States Court of Appeals for the Fifth Circuit in *Texas Eastern Transmission Corp., et al. v. Federal Energy Regulatory Commission*, Nos. 83-4390, 83-4162, and 85-4182.

## OPINION AND ORDERS BELOW

The August 19, 1985 decision of the court of appeals and its October 17, 1985 order denying petitions for rehearing of Section III of that decision are not yet reported. The Declaratory Order of the Federal Energy

Regulatory Commission ("FERC" or "Commission") is reported at 22 FERC ¶ 61,013 (1983) and the Commission's order on rehearing is reported at 24 FERC ¶ 61,004 (1983). These orders are reprinted in an appendix to the petition for a writ of certiorari filed by Transcontinental Gas Pipe Line Corporation, *et al.* ("Pipelines' Petition"), (App. ———).

## JURISDICTION

The judgment of the court of appeals was entered on August 19, 1985. The order denying petitions for rehearing was entered on October 17, 1985.

The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1).

## STATUTE INVOLVED

The statute upon which the court of appeals' decision is based is the Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3301-3432 (1982) ("NGPA"), the relevant portions of which appear in the appendix to the Pipelines' Petition (App. ——). Section 504(a)(1) of the NGPA provides that:

> (a) *General rule.*—It shall be unlawful for any person—
>
> (1) to sell natural gas at a first sale price in excess of any applicable maximum lawful price under this chapter. . .

15 U.S.C. § 3414 (1982).

## STATEMENT OF THE CASE

### A. Factual Background

Title I of the NGPA establishes maximum lawful prices for price regulated first sales of natural gas.[1] 15 U.S.C. §§ 3311-20. Under Section 504 of the NGPA, it

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[1] A "sale" is defined in Section 2(20) of the NGPA as "any sale, exchange, or other transfer for value." 15 U.S.C. § 3301(20). "First sales" generally include sales by natural gas producers and other sales at the wellhead. *See* 15 U.S.C. § 3301(21).

is unlawful for any person "to sell natural gas at a first sale price in excess of any applicable maximum lawful price." 15 U.S.C. § 3414.

Natural gas producers are generally paid for their gas in monetary form. Frequently, however, the producer receives additional payment in other forms. For example, the producer may receive payment for gas *not* delivered, or may receive free services and other non-monetary consideration. At issue in this case is one type of service frequently performed by pipeline purchasers for producers in consideration for sales of natural gas: the transportation and handling of natural gas liquids and liquefiable hydrocarbons owned by the producer.

When natural gas flows from a well, the gas stream typically includes valuable substances other than methane (the primary constituent of the gas delivered to natural gas consumers). These substances include heavy gaseous hydrocarbons that can be liquefied, and liquid hydrocarbons (oil). In many cases, the producer reserves title to these "liquids or liquefiables" and sells them to others after removal from the gas stream. Declaratory Order at 61021, (App. —). In many cases also, the pipeline purchaser of the gas provides free or underpriced transportation and handling of the liquids and liquefiables for the producer. As the FERC acknowledged in the orders affirmed by the court of appeals, these services constitute "consideration flowing to the producer," the value of which "may very well" "exceed[] the applicable Title I ceiling price for the natural gas." Declaratory Order at 61023, (App. —); Order Denying Rehearing at 61027 n.39 (App. —).

**B. Procedural History**

In mid-1981, Petitioners and other parties requested a Commission ruling on the relationship between NGPA ceiling prices and free or underpriced pipeline transportation of producer-owned liquids and liquefiables. On

January 17, 1983, the Commission, without conducting any evidentiary proceedings or inviting briefs on the question, issued a Declaratory Order, holding that free or underpriced transportation of producer-owned liquids and liquefiables does not constitute part of the price paid for natural gas. Although the Commission conceded that receipt of some forms of non-monetary consideration (for example, gemstones or real estate) in addition to the maximum lawful price ("MLP") for the gas sold would violate Title I of the NGPA (Declaratory Order at 61027 n. 21 (App. ——)), the Commission concluded that receipt of free or underpriced transportation of liquids and liquefiables in addition to the MLP would not. *Id.* at 61025 (App. ——).

The court of appeals affirmed the Commission, and it is from this decision that Petitioners seek to appeal.

## SUMMARY OF REASONS FOR GRANTING THE PETITION

The Fifth Circuit's decision erroneously affirms the Commission's declaration that natural gas producers may receive the maximum lawful price allowed under the NGPA in cash, *and also* receive additional value in the form of free or underpriced transportation services provided by the pipeline purchaser. This holding is contrary to the plain language of the NGPA, undermines the ceiling price structure established by Congress in that Act, and will permit natural gas producers to retain substantial windfall profits in excess of the consideration permitted by Congress. Moreover, this decision is inconsistent with the Commission's own finding in the same Declaratory Order that *some* forms of non-monetary consideration for the sale of gas (*e.g.*, gemstones and real estate) received in addition to the MLP would violate the NGPA. Section III of the court of appeals' opinion, therefore, decides an important question of federal law which has not been, but should be, settled by this Court.

## REASONS FOR GRANTING THE PETITION

### I. The Court Of Appeals' Decision Is Contrary To The Plain Language Of The NGPA, Invites Circumvention Of NGPA Ceiling Price Limitations, And Is Internally Inconsistent.

The NGPA does not limit the term "price" to monetary consideration only. There is no indication in the statute or its legislative history that Congress intended to depart from the widely applied principle that the price paid for goods includes non-monetary consideration, including services.[2] On the contrary, in order to eliminate loopholes that might permit sellers to circumvent ceiling prices, the NGPA itself defines the term "sale"—applied in the statutory phrase "first sale price"—broadly to include transactions in which natural gas is sold in exchange for non-monetary consideration. NGPA § 2(20), 15 U.S.C. § 3301(20) (sales include "any sale, exchange, or other transfer for value").[3]

The Commission's and the Fifth Circuit's decisions invite circumvention of the NGPA Title I ceiling price pro-

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[2] Under the Interstate Commerce Act, for example, it is unlawful for a shipper to pay any transportation rate other than the rate lawfully filed with the Interstate Commerce Commission. 49 U.S.C. § 11903(a). This Court has held that price "concessions are none the less illegal, if made for non-transportation *services*, as long as they result in lowering directly or indirectly transportation costs to the shipper." *Union Pacific R. Co. v. United States*, 313 U.S. 450, 464 (1941) (emphasis added). *See United States v. Food Fair Stores, Inc.*, 417 F.2d 62, 64 (5th Cir. 1969). Similarly, for purposes of "price discrimination" under the antitrust laws, price has been defined to include all forms of monetary and non-monetary consideration including services. *See Indian Coffee Corp. v. Procter & Gamble Co., Inc.*, 482 F. Supp. 1104, 1107-08 (W.D. Pa. 1980) (collecting cases).

[3] Moreover, NGPA § 2(21)(A)(v) expressly authorizes the Commission to expand even further the definition of first sales "in order to prevent circumvention of any maximum lawful price established under this chapter." 15 U.S.C. § 3301(21)(A)(v).

visions not only with respect to the transportation services at issue in this case but also other forms of non-monetary consideration as well. The Court acknowledged this in its opinion:

> [T]he Commission's orders below admittedly raise . . . the specter of opening a gaping loophole in the maximum lawful price provisions in the NGPA. As the Pipelines argue, and with some force, there is considerable frailty in a definition of price that includes money and other tangible property but excludes service of unquestioned value.

August 19, 1985 Opinion at 30 (App. —).

## II. The Court Of Appeals' Reasons For Affirming The Commission's Declaratory Order Have No Support In The NGPA Or Its Legislative History.

The Court nonetheless upheld the Commission's orders authorizing the receipt of a natural gas price, including money and services, exceeding the maximum lawful price. The principal basis for its decision was the Court's conclusion that consumers can be protected from the impact of overpriced gas through cost allocation in pipeline rate proceedings under Section 4 of the Natural Gas Act, 15 U.S.C. § 717(c):[4]

> On the special facts of this case, however, the order of the Commission can be sustained. This is so, because the Commission has had a longstanding policy of requiring that pipelines not allocate these costs to the consumer in their rate proceedings. . .

August 19, 1985 Opinion, at 30. Thus, the court approved the violation of congressionally mandated ceiling prices on the ground that the impact of the violation

---

[4] AGD does not concede that cost allocation in rate proceedings adequately protects the ultimate consumers of natural gas from excess prices paid to natural gas producers. That issue, however, has no bearing on whether NGPA price ceilings have been violated.

could be mitigated in separate proceedings under a different Act.[5]

The Court's decision is contrary to the clear requirements of the NGPA. Section 504 of the NGPA makes it unlawful for any person "to sell natural gas at a first sale price in excess of any applicable maximum price." 15 U.S.C. § 3414. *See INGAA v. FERC*, 716 F.2d 1, 15 (D.C. Cir. 1983), *cert. denied*, 104 S. Ct. 1615 (1984); *Pennzoil Co. v. FERC*, 645 F.2d 360, 375-76 (5th Cir. 1981), *cert. denied*, 454 U.S. 1142 (1982). Section 504 contains no exceptions. It does *not* state that a price in excess of the maximum lawful price may be charged where the Commission or the courts believe that consumers can be protected in collateral proceedings under a different Act. The Commission's duty to enforce NGPA price ceilings is absolute.

Moreover, the Commission's authority to adjust those price ceilings is strictly limited.[6] Thus, the Commission

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[5] The Court was also "unpersuaded that Congress intended the Commission to consider this particular service as part of the price." August 19, 1985 Opinion, at 31 (App. ——). Thus, the Court appeared to assume that valuable consideration should not be considered a part of price unless Congress specifically addressed the type of consideration at issue.

However, the NGPA establishes *precise* price ceilings applicable to first sales of natural gas, and the court of appeals acknowledges that the exclusion of free services from consideration as an element of price creates "a gaping loophole" in this regulatory scheme. Given the comprehensive price regulation provisions established by Congress in the NGPA, the court should have assumed that *all* elements of price are regulated in the absence of specific evidence that an exception was intended. *Cf. Public Service Commission v. Mid-Louisiana Gas Co.*, 463 U.S. 319, 336 (1983) ("Given such a comprehensive scheme, we conclude that Congress would have clearly identified, either in the statutory language or in the legislative history, any significant source of production that was intended to be excluded.")

[6] *See Public Service Commission v. Mid-Louisiana Gas Co.*, 463 U.S. 319, 331 (1983) (The NGPA "is designed to supplant the Commission's authority to establish rates for the wholesale market, the market consisting of so-called 'first sales' of natural gas.").

is authorized to establish maximum lawful prices in excess of congressionally-mandated price ceilings only in specific narrowly defined circumstances. Section 107(b) of the NGPA, for example, provides that:

> The Commission may, by rule or order, prescribe a maximum lawful price applicable to any first sale of any high-cost natural gas which exceeds the otherwise applicable maximum lawful price to the extent that such special price is necessary to provide reasonable incentives for the production of such high-cost natural gas.

15 U.S.C. 3317(b). Similarly, Sections 104(b)(2), 106(c) and 109(b)(2) authorize the Commission to raise price ceilings for certain categories of gas when the Commission determines that a higher price is "just and reasonable" under the Natural Gas Act. 15 U.S.C. §§ 3314(b)(2), 3316(c), 3319(b)(2). Finally, Section 110 provides special allowances for the recovery of severance taxes and certain production-related costs. 15 U.S.C. § 3320.

None of these circumstances is applicable here. The Commission did not assert that the instant departure from NGPA ceiling prices was necessary to allow the recovery of production-related costs, nor did it rationalize its order in terms of the rate increase authority prescribed in NGPA Sections 104, 106, 107 and 109. In short, the Commission does not even contend that any of the narrowly defined exceptions to the NGPA Title I maximum lawful price ceilings applies to the producers' receipt of money and services when the total value received exceeds the applicable NGPA ceiling price.

In this case, the Commission and the court of appeals acknowledge that natural gas producers in some circumstances violate Title I of the NGPA by selling gas at a price, including money and other forms of payment, in excess of the maximum lawful price. Neither the Commission nor the Courts may authorize a violation of Title

I, even where they believe that consumers may ultimately be protected from the impact of this violation in separate proceedings under a different Act. The Commission's Declaratory Order is in conflict with the clear language of the NGPA, invites circumvention of NGPA ceiling price limitations, would permit substantial windfall profits not intended by Congress, and is internally inconsistent. Section III of the court of appeals' opinion affirming the Commission's Declaratory Order decides an important question of federal law which has not been, but should be, settled by this Court.

## CONCLUSION

For the foregoing reasons, AGD requests that its petition for a writ of certiorari be granted.

Respectfully submitted,

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January 15, 1986

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# APPENDIX

## APPENDIX

### ASSOCIATED GAS DISTRIBUTORS

Atlanta Gas Light Company

Subsidiaries:

Georgia Gas Company
Georgia Engine Sales & Service Co.
Trustees Investments, Inc.

Baltimore Gas & Electric Company

Subsidiaries:

Safe Harbor Water Power Corporation
Diversfied Holdings, Inc.

Subsidiaries:

Baltimore Biogas, Inc.
Baltimore Capital Resources, Inc.
Resource & Property Management, Inc.

Bay State Gas Company

Subsidiaries:

Bay State Energy Resources, Inc.
Bay State Exploration, Inc.
Bay State Gas Supply, Inc.
Northern Utilities, Inc.

Subsidiary:

Granite State Gas Transmission, Inc.

The Berkshire Gas Company

Boston Gas Company

Parent: Eastern Gas and Fuel Associates

The Brooklyn Union Gas Company

Subsidiaries:

Fuel Resources, Inc.
Gas Energy, Inc.
Star Enterprises, Inc.
Methane Development Corp.

Affiliate: Honeoye Storage Corp.

Central Hudson Gas & Electric Corporation

Subsidiaries:

Central Hudson Enterprises Corp.
Central Hudson Cogeneration, Inc.
CH Resources, Inc.
Greene Point Development Corp.
Phoenix Development Co., Inc.

Chesapeake Utilities Corporation

Subsidiary:

Eastern Shore Natural Gas Co.

Subsidiaries:

Dover Exploration Co.
Skipjack, Inc.
Sharpgas, Inc.

City of Holyoke, Mass., Gas & Electric Department

City of Norwich, Dept. of Public Utilities

City of Westfield Gas & Electric Light Department

Colonial Gas Company

Subsidiaries:

Transgas, Inc. (Mass.)
Massachusetts Associates, Inc. (Mass.)

Commonwealth Gas Co.

Parent: Commonwealth Energy System

Concord Natural Gas Corporation

Subsidiary: Concord Gas Service Corp.

Consolidated Edison Company of New York, Inc.

Delmarva Power & Light Company

Subsidiaries:

Delmarva Energy Company
Delmarva Industries, Inc.
Delmarva Capital Investments, Inc.

Subsidiary: DCII, Inc.

Elizabethtown Gas Company

Parent: NUI Corporation

EnergyNorth, Inc.

Subsidiaries:

Gas Service, Inc.

Subsidiary: Energy Resources Corp.

Manchester Gas Co.

Subsidiaries:

Rent-A-Space of New England, Inc.
EnergyNorth Realty, Inc.

Essex County Gas Company

Fitchburg Gas & Electric Light Company

Subsidiary: Fitchburg Energy Development Co.

Lynchburg Gas Company

Subsidiary: Lynco Development Corp.

New Jersey Natural Gas Company

Parent: New Jersey Resources Corporation

New York State Electric & Gas Corporation

Subsidiary: Somerset Railroad Corporation

North Carolina Natural Gas Corporation

Subsidiaries:

NCNG Exploration Corp.
Cape Fear Energy Corp.

Northeast Georgia Municipal Gas Utilities

City of Bowman, Ga.
City of Buford, Ga.
City of Commerce, Ga.
City of Covington, Ga.
City of Elberton, Ga.
City of Hartwell, Ga.
City of Lawrenceville, Ga.
City of Madison, Ga.
City of Monroe, Ga.
City of Royston, Ga.
City of Social Circle, Ga.
City of Sugar Hill, Ga.
City of Toccoa, Ga.
City of Union Point, Ga.
City of Winder, Ga.

Subsidiaries:

The Connecticut Light & Power Co.
Western Massachusetts Electric Co.
Holyoke Water Power Company
Northeast Utilities Service Co.
Northeast Nuclear Energy Co.

Northern Utilities, Inc.

See Bay State Gas Company

Pennsylvania Gas & Water Company

Parent: Pennsylvania Enterprises, Inc.

Pequot Gas Co.

Philadelphia Electric Company

Subsidiaries:

Adwin Equipment Company
Adwin Realty Company
Conowingo Power Company
Eastern Pennsylvania Development Company
Eastern Pennsylvania Exploration Company
Philadelphia Electric Power Company
The Susquehanna Electric Company
The Susquehanna Power Company

Philadelphia Gas Works

Providence Gas Company

Parent: Providence Energy Corporation

Public Service Company of North Carolina, Inc.

Subsidiary:

PSNC Natural Resources Corporation

Subsidiaries:

Tar Teel Energy Corp.
PSNC Production Corp.
PSNC Exploration Corp.
PSNC Propane Corp.

Public Service Electric & Gas Co.

Subsidiaries:

Energy Development Corporation

Subsidiary:

Gasdel Pipeline System, Inc.

Energy Pipeline Corporation
Energy Terminal Services Corporation
Mulberry Street Urban Renewal Corporation
PSE&G Overseas Finance N.V.
PSE&G Research Corporation

South County Gas Co.

South Jersey Gas Co.

Parent: South Jersey Industries, Inc.

The Southern Connecticut Gas Co.

Parent: Connecticut Energy Corp.

UGI Corporation

Subsidiaries:

AmeriGas, Inc.
UGI Development Co.

Valley Gas Co.

Parent: Valley Resources, Inc.

Washington Gas Light Co.

Subsidiaries:

Crab Run Gas Co.
Davenport Insulation, Incorporated

Subsidiaries:

Cellin Manufacturing, Inc.
Universal Insulation, Inc.
Featherstone Manufacturing Co., Inc.

Frederick Gas Co., Inc.
Hampshire Gas Co.
Shenandoah Gas Co.
Brandywood Estates, Inc.

Subsidiary:

Washington Gas Approved Services, Inc.

Rock Creek Properties, Inc.

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TRANSCONTINENTAL GAS PIPE LINE
CORPORATION, *ET AL.*,
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v.

FEDERAL ENERGY REGULATORY COMMISSION,
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## COUNTERSTATEMENT OF QUESTION PRESENTED

Do ceiling prices under the Natural Gas Policy Act of 1978 apply only to the natural gas as a commodity produced at the wellhead, as found by the Court of Appeals, or do the ceiling prices also include the value of transportation of liquid and liquefiable hydrocarbons provided by pipelines?

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CASE NOS. 85-1190 AND 85-1207

IN THE

# Supreme Court of the United States

OCTOBER TERM, 1985

ASSOCIATED GAS DISTRIBUTORS AND
PUBLIC SERVICE COMMISSION OF
THE STATE OF NEW YORK,
*Petitioners,*

v.

FEDERAL ENERGY REGULATORY COMMISSION,
*Respondent.*

TRANSCONTINENTAL GAS PIPE LINE
CORPORATION, *ET AL.*,
*Petitioners,*

v.

FEDERAL ENERGY REGULATORY COMMISSION,
*Respondent.*

## BRIEF IN OPPOSITION TO PETITIONS FOR A WRIT OF CERTIORARI

The undersigned producers (Producers),[1] parties to the proceedings before the Federal Energy Regulatory

1. The parties joining in this Brief are listed on the inside page of the cover. The subsidiaries and affiliates of these Companies are included in the Appendix.

Commission (Commission) and the Court of Appeals, submit this Brief in Opposition to the Petitions, in accordance with Rule 22 of this Court.[2]

## COUNTERSTATEMENT OF THE CASE

The Statement of the case presented by Petitioners Associated Gas Distributors, *et al.*[3] (AGD) and Transcontinental Gas Pipe Line Corporation, *et al.*[4] (Transco) does not reveal facts, and fails to disclose the basis for the decision of the Commission and the Court of Appeals.

A contract for the sale of natural gas by a producer to an interstate pipeline company or other purchaser consists of two basic components:

> (1) The *price* received for the commodity itself, *i.e.*, natural gas, which is produced at the wellhead, at which point the *production* operation ceases; and
>
> (2) The *services* to be performed by either the producer or the purchaser after production. These services may be necessary to gather the gas from various wells, compress it, treat the gas to remove impurities, and process the gas to remove valuable liquid or liquefiable hydrocarbons which may then be sold in liquid form. The need for these services,

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2. Sup. Ct. Rule 22.

3. The Petitioners in Case No. 85-1190 are the Associated Gas Distributors (listed in the Petition) and the Public Service Commission of the State of New York.

4. The Petitioners in Case No. 85-1207 are: ANR Pipeline Company, Interstate Natural Gas Association of America, Natural Gas Pipeline Company of America, Sea Robin Pipeline Company, Southern Natural Gas Company, Tennessee Gas Pipeline Company, Texas Eastern Transmission Corporation and United Gas Pipe Line Company.

> and the decision whether the various services are to be performed by the producer or the purchaser varies from well to well, depending on the quality and pressure and liquid content of the gas.

The Orders here at issue focus on only one of the many services capable of being performed by either producer or pipeline: *i.e.*, the transportation of the unprocessed gas, containing liquid and liquefiable hydrocarbons,[5] from the wellhead to a gas processing plant. These liquid and liquefiable hydrocarbons are extracted and the residue gas is delivered to the purchaser at the plant tailgate for resale to its customers. The Orders relate to cases where this transportation service is performed by the pipeline purchaser.

In pipeline rate proceedings, the Commission allocates a portion of these transportation costs of the unprocessed gas to the cost of transporting the portion of the common steam that is liquefied at the processing plant by the producer for its own account. By reason of this allocation, the costs attributable to the transportation of the producer's liquids and liquefiables are taken out of the rates charged to gas consumers. The Commission leaves to the contract between the parties the determination of whether some or all of these costs are recovered by the pipeline from the producer.

In some cases, the contracts provide that the compensation paid by the producer to the pipeline for the service of transporting these liquid and liquefiable hydrocarbons is less than the amount the Commission has allocated to this function in the pipeline rate cases. Petitioners here assert that the ceiling price paid for the gas as a com-

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5. *See* Transco Petition, at 3, n.3.

modity at the wellhead *must be reduced* by an amount at least equal to the difference between the consideration provided in the contract for the transportation of liquid and liquefiable hydrocarbons and the cost allocated to that function by the Commission. Otherwise, say Petitioners, the ceiling price is exceeded.

Contrary to the implication contained in Petitioners' Briefs, these contractual arrangements are not and could not be intended to circumvent the Natural Gas Policy Act of 1978 (NGPA) ceiling prices. These arrangements have been common in natural gas sales contracts for many years prior to enactment of the NGPA and before the Commission determined what portion of the transportation costs incurred by the pipelines should be allocated to the transportation of liquid and liquefiable hydrocarbons. Moreover, these contractual arrangements were lawful under the Commission's Natural Gas Act (NGA) regulation at the time of enactment of the NGPA. National rates for regulation of producer wellhead prices under the NGA did not require that a deduction be made for the cost or value of pipeline transportation of liquids and liquefiables.

Therefore, the Commission, and the Court of Appeals on review, were faced with making a decision between two opposing interpretations of the NGPA, to-wit:

> 1. Did the ceiling prices set out in the various sections of the NGPA apply only to the natural gas, as a commodity; *or*
>
> 2. Did the ceiling prices set out in the NGPA also include the downstream services performed by pipelines, such as transportation of liquids or liquefiable hydrocarbons?

After carefully weighing arguments favoring each interpretation, the Commission decided that the first interpretation of the NGPA was correct.[6] The Court of Appeals agreed with the Commission.[7]

## ARGUMENT

### A. The Basis On Which The Court Of Appeals And The Commission Reached Their Decisions Is Misconstrued And Misstated By The Petitioners.

Both AGD[8] and Transco[9] assert that the Commission's Orders rest solely on the ground that the Commission defined the "price" paid for natural gas under a gas sales contract to be limited to the monetary consideration paid to the producer, and excluded all non-monetary considerations included in the contract from the definition of the "price." Having set up this strawman, Petitioners then proceed to tear it down by arguments that "price" should include non-monetary considerations flowing to the gas producer under the contract as well.[10] Further, the Petitioners rely on their mischaracterization of the Commis-

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6. 22 FERC ¶ 61,013, App. 29a-50a, *aff'd on rehearing*, 24 FERC ¶ 61,004 (1983), App. 51a-77a.

7. Texas Eastern Transmission Corp., *et al.* v. F.E.R.C., 769 F.2d 1053, 1068-1069 (5th Cir. 1985), App. 24a-26a.

8. Petition, at 4-6.

9. Petition, at 8-19.

10. Transco Petition, at 9-10; AGD Petition, at 5. The citations to cases under the Interstate Commerce Act (at 5, n.5) are inapposite, as the rate structures under this Act are different from the price ceilings under the NGA and the NGPA. *See* United Gas Pipe Line Co. v. Mobile Gas Service Corp., 350 U.S. 332, 338-339 (1956); Pennzoil Co. v. F.E.R.C., 645 F.2d 350 (5th Cir. 1981).

sion's Order to engage in hyperbole, claiming that the Order will lead to widespread circumvention of NGPA ceilings by the use of a "loophole," *i.e.*, structuring gas sales in exchange for non-monetary consideration.[11]

The Orders below rest on an entirely different ground. In its Orders, the Commission drew a distinction, not between monetary and non-monetary types of consideration, but instead between the "price" paid for the natural gas produced at the wellhead[12] and the consideration for those *services* performed *after* the gas left the wellhead. Indeed, the Commission specifically found that non-monetary considerations, such as gemstones, metals or common stock, received for the gas itself would be taken into account in enforcing NGPA ceiling prices.[13] In assuring that circumvention of NGPA ceiling prices would not be countenanced, the Commission distinguished such artificial pricing structures involving non-monetary consideration and the transportation of liquid and liquefiable hydrocarbons that "are a traditional part of pipeline-producer contracting practices."[14]

The typical gas sales contract provides for a price *for the gas* and, *in addition*, provides for the assignment of responsibilities between the producer and the pipeline to provide various post-production services which involve costs. If the Commission were required to take these services into account, together with the price paid for the gas itself, and compare the *total* of the two to the maxi-

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11. AGD Petition, at 5; Transco Petition, at 20.

12. *See* 22 FERC ¶ 61,013, at 61,027, n.21, App. 41a.

13. *See* 24 FERC ¶ 61,004, at 61,022, App. 61a-62a.

14. *Id.*

mum lawful price,[15] the process would become, in the Commission's words, "extra-ordinarily complex."[16]

The Commission noted:

> The legislative history of the NGPA shows that Congress sought to avoid uncertainty and delay by generally pricing gas at the wellhead in simple dollar amounts. More specifically, the legislative history of the NGPA shows the maximum lawful price was for gas at the wellhead, without any offset.[17] (nn. omitted)

The Commission's view reflects this Court's observation in *Public Service Commission of the State of New York v. Mid-Louisiana Gas Company*, 463 U.S. 329, ——, (1983), that the NGPA established "a precise schedule of price ceilings. . . ."

The Commission did not rest its decision on whether the consideration paid the producer was monetary or

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15. The maximum lawful price is described in the NGPA itself as a "wellhead price." (*See* 15 U.S.C.A. § 3311, title to Subchapter and again to Part A thereof.)

16. 22 FERC ¶ 61,013, at 61,024, App. 43a-44a; The Commission further stated:

> "Under AGD's and Tetco's [Transco's] reading of the NGPA, all non-monetary considerations—whether flowing from the seller or flowing from the buyer—(not just the transportation of removed substances) would have to be assigned a value. Only after the total "cost" or "value" of *all* services and considerations performed by the seller and the buyer were computed, could the net consideration paid for the gas be compared with the Title I maximum lawful price. This massively complex system of costing and valuing every quantum of consideration was plainly not intended by Congress which generally sought in Title I to spur production by setting non-cost-based, incentive ceiling prices at the wellhead." 22 FERC ¶ 61,013, at 61,024, App. 43a-44a.

17. 22 FERC ¶ 61,013, at 61,024, App. 44a.

non-monetary, but took into consideration the intent of Congress on the question of where, and to what, the maximum lawful price applied. Citing pertinent legislative history,[18] the Commission affirmed that this ceiling price was applicable only to the consideration (or "price" or "value") paid for the gas at the wellhead.[19]

On review, AGD and Transco again laid their arguments before the Court of Appeals, and were again rejected. The Court concluded that "[i]t therefore does not seem unreasonable or inconsistent with the purposes of the NGPA to require the pipelines to adhere to their contracts."[20] The Court of Appeals further stated:

> [W]e are unpersuaded that the Congress intended to require the Commission to consider this particular service as a part of the price. Accordingly, we defer to the Commission's reading of the statute.
>
> . . . .
>
> Moreover, this scheme frees the Commission from the endless chore of assigning a value to every

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18. *See* 22 FERC ¶ 61,013, at 61,028, nn. 27, 28, App. 44a.

19. The Commission reaffirmed its interpretation of the NGPA on rehearing, rejecting the same arguments made by Petitioners to this Court. The Commission stated:

> "There is really only one choice possible: an interpretation of Title I that provides certainty of pricing. This is consistent with the intent of Congress and most appropriate to carry out the Commission's functions under the NGPA. The other alternative would not have furthered these purposes and would have resulted in a massively complex, if not unenforceable, system of costing and valuing every quantum of consideration in thousands of gas purchase contracts." 24 FERC ¶ 61,004, at 61,022, App. 61a.

20. 769 F.2d 1053, 1069 (1985), App. 26a.

aspect, every covenant, every warranty in a gas contract.[21]

### B. The Commission's Interpretation Of The NGPA Is Consistent With The Commission's Practice Which Was In Place Prior To The Enactment Of The NGPA.

Transco states (at 4, n. 4) that prior to the enactment of the NGPA the Commission's practice was to require a downward adjustment in the wellhead ceiling price to reflect the value of the transportation services performed here, citing the *Southern Louisiana Area Rate Prodeeding*.[22] In its Orders, the Commission specifically refuted such a characterization of its prior practice.[23] In any

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21. App. 25a-26a. In an attempt to counter the language of the Commission's Orders and the Court of Appeals' Opinion, Transco cites a Notice of Proposed Rulemaking in another case issued two and one-half years earlier, and a brief of the Commission's Trial Staff in a recent case pending before the Commission, *see* Transco Br. at 10, n.18. Neither of these rise to the level of Commission precedent, *see* 24 FERC ¶ 61,004, at 61,025, App. 74a.

22. 46 F.P.C. 86 (1971), *aff'd*, Placid Oil Co. v. F.P.C., 483 F.2d 880 (5th Cir. 1973), *aff'd sub nom.* Mobil Oil Corp. v. F.P.C., 417 U.S. 283 (1974).

23. 24 FERC ¶ 61,004, at 61,021, App. 57a-59a. Also contrary to Transco's assertion (at 15), it cannot be inferred from Section 110 of the NGPA that Congress intended to require the Commission to include the costs or value of the transportation of liquids and liquefiables within NGPA ceiling prices. Section 110 relates only to allowances that producers may collect by Commission order for services producers provide to their purchasers. It does not relate, as do the Commission Orders at issue here, to traditional services provided to producers by pipeline purchasers. Indeed, to the extent any inference can be drawn from Section 110, it supports the Commission. The inclusion of Section 110 indicates that Congress intended that the ceiling prices prescribed in the other sections of the NGPA were intended to refer to the price of the natural gas as a commodity at the wellhead, and that the post-production services provided by producers were not covered by the ceiling prices stated in Sections 102 through 109 of the NGPA.

event, the Commission's *Southern Louisiana* decision was superseded by three *National Rate decisions*,[24] which did not provide for any downward adjustment in the ceiling prices for services performed by pipelines for producers as provided by their contracts.[25] In other words, the cost or value of liquids and liquefiables transportation was not part of the "price" for natural gas under the NGA. The failure of Congress to deal expressly with the subject creates a presumption that it did not intend to change prior Commission practice.[26]

### C. Petitioners Have Not Satisfied The Required Standard Of Review.

In *Federal Election Commission v. Democratic Senatorial Campaign Committee*,[27] this Court outlined the deference that should be accorded the interpretation of an agency, such as the Commission in this case, in which Congress has vested primary and substantial responsibility

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24. First National Rate Case For New Gas, 52 F.P.C. 1604 (1974), *aff'd sub nom.* Shell Oil Co. v. F.P.C., 520 F.2d 1061 (5th Cir. 1975), *rehearing denied*, 525 F.2d 1261 (5th Cir. 1976), *cert. denied sub nom.* California Co. v. F.P.C., 426 U.S. 941 (1976); Second National Rate Case For New Gas, 56 F.P.C. 509 (1976), *on rehearing*, 56 F.P.C. 2698 (1976), *aff'd*, American Public Gas Ass'n v. F.P.C., 567 F.2d 1016 (D.C. Cir. 1977), *cert. denied* 435 U.S. 907 (1978); and National Rate Case For Flowing Gas, 54 F.P.C. 3090 (1975), *aff'd*, Tenneco Oil Co. v. F.E.R.C., 571 F.2d 834 (5th Cir. 1978), *cert. dismissed*, 439 U.S. 801 (1978).

25. *See* Second National Rate Case, 56 F.P.C. 2698, 2807-2809; *see also* 18 C.F.R. § 2.56b(d) and (e).

26. Interstate Natural Gas Ass'n of America v. F.E.R.C., 716 F.2d 1 (D.C. Cir. 1983), *cert. denied*, 465 U.S. 1108 (1984). *See also* Public Service Comm'n of New York v. Mid-Louisiana Gas Co., 463 U.S. 319 (1983).

27. 454 U.S. 27 (1981).

for administering and enforcing a statute. There, this Court stated that:

> [T]he task for the Court of Appeals was not to interpret the statute as it thought best but rather the narrower inquiry into whether the Commission's construction was "sufficiently reasonable" to be accepted by a reviewing court . . . to satisfy this standard it is not necessary for a court to find that the agency's construction was the only reasonable one or even the reading the court would have reached if the question initially had arisen in a judicial proceeding.[28]

If this Court finds that "the statute is silent or ambiguous with respect to the specific issue, the question for this Court is whether the agency's answer is based on a permissible construction of the statute."[29] This Court also has stated "that the construction of a statute by those charged with its execution should be followed unless there are compelling indications that it is wrong."[30]

Deference given by the Court of Appeals to the Commission's construction of the NGPA was particularly appropriate in this case. The Commission has express statutory authority to define terms used in the NGPA.[31] The Court of Appeals found that the Commission's inter-

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28. *Id.*, at 39. *See also* Udall v. Tallman, 380 U.S. 1, 16 (1965).

29. Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837, _____, 104 S. Ct. 2778, 2781-83, 81 L.Ed.2d 694, 703-04 (1984); Chemical Manufacturer's Association v. Natural Resources Defense Council, Inc., _____U.S._____, 105 S. Ct. 1102, 1108 (1985).

30. Red Lion Broadcasting Co. v. F.C.C., 395 U.S. 367, 381 (1969).

31. Section 501(b) of the NGPA, 15 U.S.C. § 3411(b).

pretation is reasonable.[32] The Commission's construction can have no impact on the consumers of natural gas. By allocating the cost of transporting liquid and liquefiable hydrocarbons out of the pipeline's rate base, the Commission has made sure that none of those costs will be paid by gas consumers.[33] The pipeline purchaser is merely held to the provisions of its contract, as the Court of Appeals noted below.[34]

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32. 769 F.2d 1053, 1069 (1985), App. 26a. Transco devotes an entire section of its Petition (at 16-18) to a red herring argument that the Commission's Order preempts state contract law by its definition of "price" and "transfer for value" in the NGPA. On the contrary, it is Transco which seeks to avoid the clear provision of its contract by an interpretation of the NGPA ceiling prices which reduces the price for the gas received *below* that provided by the contract *and* the statute.

33. This was the method recommended by the Court of Appeals for dealing with this problem in an earlier case, *see* Mobil Oil Corp. v. F.P.C., 483 F.2d 1238, 1243 (D.C. Cir. 1973).

34. 729 F.2d 1053, 1069 (5th Cir. 1985), App. 26a.

## CONCLUSION

No valid grounds exist for review by this Court of the interpretation of the NGPA adopted by the Commission and affirmed by the Court of Appeals. This interpretation is reasonable, consistent with Congressional intent, and within the area of discretionary expertise which is subject to limited Court review. The Petitions for Certiorari should be denied.

Respectfully submitted,

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February 14, 1986

## APPENDIX A

### LIST OF PARENT COMPANIES, SUBSIDIARIES AND AFFILIATES REQUIRED BY RULE 28.1

Pursuant to Rule 28.1, Producers list their parent companies, subsidiaries (other than wholly-owned subsidiaries) and affiliates. This list is limited to entities with stock or debt securities publicly traded in the United States or Canada:

### AMERADA HESS CORPORATION

Amerada Hess Corporation has no subsidiaries or affiliates.

### AMOCO PRODUCTION COMPANY

Amoco Production Company is a wholly-owned subsidary of Amoco Corporation. The subsidiaries and affiliates (not wholly owned by Amoco Corporation or a wholly-owned subsidiary) of Amoco Production Company are:

Amoco Australia Limited
Amoco Canada Petroleum Company, Ltd.
Amoco Credit Corporation
Amoco Oil Holdings S.A.
Amoco (U.K.) Exploration Company
Analog Devices Inc.
Cetus Corporation
Cyprus Mines Corporation

### ARCO OIL AND GAS COMPANY

ARCO Oil an Gas Company is a division of Atlantic Richfield Company. The subsidiaries and affiliates (not wholly owned) of Atlantic Richfield Company are:

Alyeska Pipeline Service Company
Anamax Mining Company
Badger Pipeline Company
Black Lake Pipe Line Company
Caribou-Chaleur Bay Mines Ltd.
Colonial Pipeline Company
Cook Inlet Pipe Line Company
Dixie Pipeline Company
East Texas Salt Water Disposal Company
85819 Canada Limited
Eisenhower Mining Company
Flower Street Limited
Kenai Pipe Line Company
Kuparuk Transportation Company
Las Quintas Serenas Water Company
Park Cummings Mining Company
Park-Premier Mining Company
Platte Pipe Line Company
Prince Consolidated Mining Company
Rodman, Inc.
Smoke House Copper Mining Company
Tecumseh Pipe Line Company
Texas-New Mexico Pipe Line Company

## ASHLAND EXPLORATION, INC.

Ashland Exploration, Inc. has the following parent companies, subsidiaries (except wholly-owned subsidiaries) and affiliates:

Arch Mineral Corporation
Ashland Coal, Inc.
Ashland Oil, Inc.
Establissement Locab
Super Mom's Kitchens, Inc.
B.V. Ashland-Suedchemie v/h Necof
CARBOGAL-Carbonos de Portugal S.A.R.L.
Datacare, Inc.
Gravecap, Inc.
Iberia Ashland Chemical S.A.

Locap, Inc.
LOOP, Inc.
Melamine Chemicals, Inc.
Minnesota Pipe Line Company
Saudi Industrial Resins Limited
Tecumseh Pipe Line Company
United Carbon India Limited
Australian Carbon Black Pty. Ltd.
Malaysian Carbon Sdn. Bhd.
P.T. Indocarb
Negroven, S.A.
Applied Chemical Products (Pty) Ltd.
Applied Agricultural Products (Pty) Ltd.
Applied Foundry Products (Pty) Ltd.
Applied Industrial Products (Pty) Ltd.
Chematron Products (Pty) Ltda.
Ashland-Avebene
Ashland Croda Pty. Ltd.
Ashland de Mexico S.A. de C.V.
Ashland Resinas Sinteticas, Ltd.
Ashland-Suedchemic-Kernfest GmbH
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Kernfest-Webac, A.B.
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Medicine Bow Coal Company
Cumberland Materials, Inc.
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500 Cary Corporation
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Botswana RST Limited
Britamco Ltd.
Canada Tungsten Mining Corporation Limited
Canamax Resources, Inc.
Canyon Reef Carriers, Inc.
Cetus Corporation
Chicago Wire Goods Co. - H/FP
China Gulf Oil Company, Ltd.
Colonial Pipeline Company
Componentes Industriales Mexicandes, S.A.
Electronic Marketing Systems, Inc.
Emery Joint Venture
Explorer Pipeline Company
Felix Oil Company
Fresnillo Companies
G.S. Equipment & General Supply
General Atomic Europe Development Corp.
Gulf Oil Financial Corporation
Gulf Oil Realty Company 819
Gulf Oil Zaire S.A.R.L.
Harshaw-Bryce & Co. Pty. Ltd. - H/FP

Harshaw Chemical of Canada, Ltd. - H/FP
Harshaw Chemicals Limited - H/FP 381
Harshaw Chemie B.V. - H/FP 549
Harshaw Chemie G.M.B.H. - H/FP
Harshaw/Filtrol Partnership - H/FP 325-762
Harshaw Galvanotecnia S.A. - H/FP
Harshaw Holland N.V. - H/FP
Harshaw International Corporation - Disc
Harshaw - Juarez S.A. De C.V. - H/FP
Harshaw - Murata Kabushiki Kaisha - H/FP
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Industrial Nickel, Inc. - H/FP
Kentucky Agricultural Energy Corporation
Keydril (Nigeria) Ltd.
Kuwait Oil Company Limited
Lancer Chemical Corporation - H/FP
Laurel Pipeline Company
Long Beach Oil Development Company
Midwest Carbide Corporation
North River Energy Company
NOVA, an Alberta Corporation
Oklahoma Nitrogen Company
Pembroke Capital Company
Pembroke Cracking Company
Produtos Quimicos Somox, Ltda. - H/FP
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Rio Blanco Oil Shale Part.
Rosario Mexico S.A. de C.V.
Sarni Spa - Refining 579
Solvent Refined Coal International, Inc.
Stibium, Inc. H/FP
Transinsco Inc.
Transocean Group Inc.
UNC Resources, Inc.
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## CITIES SERVICE OIL AND GAS CORPORATION

Cities Service Oil and Gas Corporation is a wholly-owned subsidiary of Cities Service Company, which is, in turn, a wholly-owned subsidiary of Occidental Petroleum Corporation. Its non-wholly owned affiliates are:

Canadian Occidental Of California, Inc.
Southland Corporation

## CONOCO, INC.

Conoco Inc. is a wholly-owned subsidiary of E.I. du Pont de Nemours and Company. The subsidiaries and affiliates (not wholly owned) of Conoco Inc. are:

Cit-Con Oil Corporation (Delaware)
Juliana Coal Co. (Partnership)
Coman I Limited (Partnership)
Coman II Limited (Partnership)
Coman III Limited (Partnership)
Conch L.N.G. (New Jersey)
Conoco Exploration, Ltd. (Partnership)
Continental Oil Limited (Partnership)
Conrhein Coal Co. (Partnership)
Cardinal River Coals, Ltd. (Alberta, Canada)
Harmar Coal Co. (Pennsylvania)
Tongue River Railroad (Partnership)
Oasis Oil Co. of Libya, Inc. (Delaware)
Colonial Pipeline Company (Delaware)
Milne Point Pipe Line Co. (Partnership)
Dixie Pipeline Company (Delaware)
Explorer Pipeline Company (Delaware)
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Jupiter Chemicals, Inc. (Delaware)
Kettleman North Dome Assoc. (California)
Petroleum Terminals, Inc. (Indiana)

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The Standard Shale Products Company (Colorado)
Neptune Bulk Terminals (Canada) Ltd. (Canada)
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## DIAMOND SHAMROCK EXPLORATION COMPANY

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## HUNT OIL COMPANY

Hunt Oil Company is a privately-owned corporation, which is wholly-owned by Hunt Consolidated Resources Corporation, which is wholly owned by Hunt Financial Corporation. The only subsidiaries of Hunt Oil Company are:

Portal Pipeline Company
Palomo Pipeline Company

## INEXCO OIL COMPANY

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## KERR-McGEE CORPORATION

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Marathon Oil Company is a wholly-owned subsidiary of United States Steel Corporation. The subsidiaries and affiliates of Marathon Oil Company are:

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LOOP, Inc.
Locap, Inc.

## MITCHELL ENERGY CORPORATION

Mitchell Energy Corporation has no affiliated companies which are not wholly owned.

## MOBIL OIL CORPORATION MOBIL OIL EXPLORATION & PRODUCING SOUTHEAST INC., MOBIL PRODUCING TEXAS & NEW MEXICO INC. and THE SUPERIOR OIL COMPANY

Mobil Oil Corporation, Mobil Oil Exploration & Producing Southeast Inc., Mobil Producing Texas & New Mexico Inc. and The Superior Oil Company are wholly-owned subsidiaries of Mobil Corporation. The subsidiaries and affiliates of Mobil Oil Corporation or Mobil Corporation, whose securities are available for purchase by United States citizens, are:

Marcor Inc.
Mobil Alaska Pipeline Company
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## MONSANTO OIL COMPANY

Monsanto Oil Company is a wholly-owned subsidiary of Monsanto Company. Monsanto Oil Company has no subsidiaries or affiliates which are not wholly owned.

## PENNZOIL COMPANY
## PENNZOIL PRODUCING COMPANY
## PENNZOIL OIL & GAS, INC.
## PENNZOIL LOUISIANA AND TEXAS OFFSHORE, INC.

The subsidiaries and affiliates (not wholly owned) of Pennzoil Company are:

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Industrias Negromex, S.A. de CV
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## PLACID OIL COMPANY

Placid Oil Company is a privately-owned corporation. Placid Oil Company has no subsidiaries or affiliates which are not wholly owned.

## SHELL OIL COMPANY

Shell Offshore Inc. and Shell Western E&P Inc. are wholly-owned subsidiaries of Shell Oil Company.

Shell Oil Company wholly owns all of the stock of Scallop Coal Corporation and Shell Energy Resources Inc., which company wholly owns all of the stock of Pecten International Company, Shell California Production Inc., Shell Offshore Inc., Shell Mining Company and Shell Western E&P Inc. All of Shell Oil Company's common stock is owned by SPNV Holdings, Inc., a Delaware corporation, whose stock is owned by Shell Petroleum N.V., a Netherlands company. The voting shares of Shell Petroleum N.V. are held sixty percent (60%) by Royal Dutch Petroleum Company and forty percent (40%) by Shell Transport and Trading Company, a Public Limited Company in London, U.K. Shell Oil Company also wholly owns directly or indirectly a number of companies. The following companies are affiliated with Shell Oil Company or one of the affiliates named above, but are not wholly-owned subsidiaries:

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First Harlem Securities Corporation
Fractionation Research, Inc.
Gravcap, Inc.
Heat Transfer Research, Inc.
Inland Corporation
LOOP, Inc.
MESBIC Financial Corporation of Houston
Oil Companies Institute for Marine Pollution Compensation Limited
Oil Insurance Limited
Pioneer Equipment Co.
Seadock, Inc.
Pecten Cameroon Company

Thums Long Beach Company
East Texas Salt Water Disposal Company
Grande Ecallie Land Company, Inc.
Van Salt Water Disposal Company
Wyoming Industrial Development Corporation
Cortez Capital Corporation
Plastibeton, Inc.
Butte Pipe Line Company
Dixie Pipeline Company
Explorer Pipeline Company
LOCAP, Inc.
Olympic Pipe Line Company
Plantation Pipe Line Company
West Shore Pipe Line Company
Wolverine Pipe Line Company
Lone Star Polymer Concrete Corporation
General Hydrocarbon Polymer Concrete Inc.
Polycon Research, Inc.
Morrison Molded Fiber Glass Company
Premix/E.M.S. Inc.
Knytex, Inc.
CRI Ventures, Inc.
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Glass-Steel, Inc.
Huntsman Chemical Company
Lucky Chance Mining Company, Inc.
George Neuman and Company
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Suncor Inc.
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Athabasca Realty Company Limited
Baron Petroleums Inc.
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Carnduff Gas Limited
Gow Fuels Inc.
Maywelie Properties Ltd.
Nottingham Gas Limited
NOVA, an Alberta Corporation
Ouimet-Gobeille Inc.
Pacgas Limited
Redwater Water Disposal Company Limited
SMS Petroleums Ltd.
Sultran Ltd.
Sun-Canadian Pipe Line Company Limited
Sun Oil Company of Canada Limited
Suncor Supply Limited
Sunoco Home Comfort Inc.
Muskoka Oil Company Limited
Sunoco Inc.
Chemsun Inc.
Fair Wind Shipping Inc.
Solartech Limited
Sunchem Inc.
Sunchem Shipping Inc.
Sunchem (U.K.) Limited
Trillium Exploration Corporation
Canyon Reef Carriers, Inc.
East Texas Salt Water Disposal Company
Van Salt Water Disposal Company
Lavan Petroleum Company (LAPCO)
Sunray Nigeria Oil Company Unlimited
Venezoil, C.A.
Convenience Store Distributing Company
Sunolin Chemical Company
Hemisphere Oil Company, Inc. - Puerto Rico
Japan Sun Oil Company, Ltd. (Japan)
Lugrasa, S.A. (Panama)

Alaska Bulk Carriers, Inc.
Glacier Bay Transportation Corporation
Explorer Pipeline Company
Inland Corporation
Mid-Valley Pipeline Company
West Texas Gulf Pipe Line Company
White River Shale Oil Corporation
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The VLM Corporation
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## TENNECO OIL COMPANY

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A/S Haustrup-Ekco Aluminum-Emballage
Adela Investment Company, S.A.
Akulu Chemicals (Pty.) Limited
Akulu Marchon (Pty.) Limited
Albright & Wilson (Australia), Ltd.
Albright & Wilson Match Phosphorus Company Ltd.
Albright, Morarji and Pandit Limited (India)
Alcan Ekco Limited
Almi S.A.
American Synthetic Rubber Corporation
Arndale Fuels, Ltd.
Border Gas Inc.
Bracey Petroleum Products, Ltd.
Butler Oil Products Ltd.
COFAP
Case Vibromax GMBH
Collins Pipeline Company
Consolidated Diesel Company
Constructions Mecaniques De Carvin
Corax-Trac S.A.
Deepsea Ventures, Inc.
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Elston Oils Limited
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F.C. Marine, Inc.
HT Gathering Company
Indonesian Enterprises, Inc.
Intertrac Viehmann & Co.
John Oil Limited
Kern Island Water Company
Kern River Canal and Irrigating Company
Kern River Gas Supply Corporation
Kern River Service Corporation
Marchon-Paragon Sulphonation (Pty.) Ltd.
Materiel Poclain Du Sud Est.
Meaux-Materiel
Mesbic Financial Corporation of Houston
Mil Potrero Mutual Water Company
Mistal Inc.
Monroe Auto Pecas S.A.
Nuodex S.A. Industria E Comercia De Se Cantes
Oasis Pipeline Company
Oil Insurance Limited
P.P.M. Guindastes Hidraulicos S.A.
Poclain S.A.
Poclain Canada Ltee
Poclain Hydraulics, S.A.
Poclain Hydraulics Ireland
Poclain Italiana S.P.A.
Poclain Mexicana, S.A.
Polyphosphates Inc.
Potain-Poclain-Materiel, S.A.
S.A. Paper Chemicals Company
(Proprietary) Limited
STDCO Mutual Water and Sewer Company
Skogstre A/S (Norway)
Societe Financiere D'Études Et De Gerance
Societe Mecanique Automobile De Touraine
Societe Mecanique De Tournai
Southern Facilities, Inc.

T & M Terminal Company
Talleres Unidos, S.A.
Tees Storage Limited
Tenn-USS Chemicals Company
Tenngasco Gas Gathering Company
Toyo Ekco Company, Ltd. (Toyo Ekco Kabushiki Kaisha)
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Vibromax SCI

## TEXACO INC.

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Texaco Mexicana S.A. de C.V.
Duetsche Texaco Aktiengesellschaft, S.I.A.M.
Texaco Togo
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Kaneb Services, Inc.
Magma Power Company
Union Exploration Partners, Ltd.

(3) (3)

Nos. 85-1190 and 85-1207

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# In the Supreme Court of the United States

OCTOBER TERM, 1985

ASSOCIATED GAS DISTRIBUTORS AND PUBLIC SERVICE COMMISSION OF NEW YORK, PETITIONERS

*v.*

FEDERAL ENERGY REGULATORY COMMISSION

TRANSCONTINENTAL GAS PIPE LINE CORP., ET AL., PETITIONERS

*v.*

FEDERAL ENERGY REGULATORY COMMISSION

*ON PETITIONS FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT*

## BRIEF FOR THE FEDERAL ENERGY REGULATORY COMMISSION IN OPPOSITION

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30 pp

## QUESTION PRESENTED

Whether the Federal Energy Regulatory Commission acted reasonably in determining that, under the Natural Gas Policy Act of 1978, the "price" at which natural gas is sold does not include the value to the seller of free or below-cost transportation provided by a pipeline company-purchaser for components of the gas stream retained by the seller.

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# In the Supreme Court of the United States

OCTOBER TERM, 1985

No. 85-1190

ASSOCIATED GAS DISTRIBUTORS AND PUBLIC SERVICE COMMISSION OF NEW YORK, PETITIONERS

*v.*

FEDERAL ENERGY REGULATORY COMMISSION

No. 85-1207

TRANSCONTINENTAL GAS PIPE LINE CORP., ET AL., PETITIONERS

*v.*

FEDERAL ENERGY REGULATORY COMMISSION

*ON PETITIONS FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT*

**BRIEF FOR THE FEDERAL ENERGY REGULATORY COMMISSION IN OPPOSITION**

## OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-28a) is reported at 769 F.2d 1053.[1] The order of the Federal Energy Regulatory Commission (Pet. App. 29a-50a) is reported at 22 F.E.R.C. ¶ 61,013. The Commission's order on rehearing (Pet. App. 51a-77a) is reported at 24 F.E.R.C. ¶ 61,004.

[1]References to "Pet. App." are to the appendix to the petition in No. 85-1207.

## JURISDICTION

The judgment of the court of appeals was entered on August 19, 1985, and petitions for rehearing were denied on October 17, 1985. The petitions for a writ of certiorari were filed on January 15, 1986. This Court's jurisdiction is invoked under 28 U.S.C. 1254(1).

## STATEMENT

1. The raw stream of natural gas that flows out of the ground at the wellhead often is a mixture of substances that includes a variety of hydrocarbon compounds other than the natural gas itself. Gas producers generally sell their natural gas to a pipeline company at the wellhead, but frequently retain ownership of the other hydrocarbon compounds for subsequent sale to other buyers. These other hydrocarbon compounds are referred to as "liquids and liquefiables." Pet. App. 29a-30a & n.1.

The natural gas sales contract between a gas producer and a pipeline company typically sets forth the price for the natural gas (expressed as a specific dollar amount or as a formula), and contains in addition a specification of the quantity and quality of natural gas to be delivered under the contract, a term setting forth the duration of the agreement, and provisions describing the other responsibilities of the two parties. Pet. App. 34a-35a; 7 H. Williams & C. Meyers, *Oil and Gas Law* § 741.1 (1981); see also 4 H. Williams, *Oil and Gas Law* §§ 720-737 (1985). The contract also may impose on the pipeline-purchaser the additional obligation of transporting the liquids and liquefiables (ownership of which has been retained by the producer) along with the natural gas purchased by the pipeline. Pet. App. 24a, 33a.[2]

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[2]This arrangement is advantageous to the producer because it would be uneconomical to construct at each wellhead facilities to separate the liquids and liquefiables from the natural gas. For similar reasons, it would be impractical to construct a second pipeline system to transport these substances. Pet. App. 33a.

The price that a gas producer may charge for certain categories of natural gas is regulated by the Natural Gas Policy Act of 1978 (NGPA), 15 U.S.C. 3301 *et seq.*, which sets forth ceiling prices for a "first sale" of natural gas. See *Public Service Commission* v. *Mid-Louisiana Gas Co.*, 463 U.S. 319, 333-334 (1983).[3] The statute prohibits sellers of natural gas from charging a price greater than these ceiling prices (15 U.S.C. 3414(a)(1)). The present case concerns the interrelationship between these statutory maximum prices and contract provisions requiring a pipeline-purchaser to provide free or below-cost transportation for liquids and liquefiables owned by the gas producer.

This proceeding was initiated in 1981 when several parties, including petitioners, filed petitions with the Federal Energy Regulatory Commission seeking a declaratory order regarding the method of calculating the price at which natural gas is sold for purposes of ascertaining whether the sales price exceeds the applicable statutory ceiling price. The specific issue raised by the petitions was whether the express price set forth in a sales contract must be adjusted upward when the contract requires the pipeline-purchaser to provide free or below-cost transportation for liquids and liquefiables owned by the gas producer.

The Commission concluded (Pet. App. 50a) that "the value or cost of the service performed by the pipeline-purchaser in transporting liquid and liquefiable hydrocarbons on behalf of a producer-seller is not a component part of the maximum lawful prices subject to regulation under [the NGPA]." The Commission observed that the term "price" was not defined in the NGPA (Pet. App. 32a) and referred to the prior regulatory practice under the Natural Gas Act to give content to that term in the present context.

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[3]Price controls have been eliminated for some categories of natural gas sales. See 15 U.S.C. 3331.

The Commission stated that its previous regulation of the rate at which natural gas was sold to pipelines did not include regulation of agreements between gas producers and pipelines regarding the transportation of liquids and liquefiables. The Commission instead simply ensured that gas consumers did not bear the cost of transportation of liquids and liquefiables. Thus, the effect of the Commission's action "in almost all cases [was] to leave the consideration to be paid for the transportation and handling of [liquids and liquefiables] to private contractual negotiation between the parties, but to rely upon its pipeline rate authority to assure that these costs would not be subsidized by natural gas customers" (*id.* at 37a (footnote omitted)).

The Commission determined that the enactment of the NGPA did not evince any congressional intent to alter this regulatory approach. Since the cost of transporting liquids and liquefiables previously had not been regulated as part of producer-pipeline natural gas sales transactions, the Commission concluded that Congress did not intend to require that these costs be considered in calculating the "price" received for natural gas by the producer for purposes of assessing whether the transaction complied with the price ceiling established by the NGPA. Pet. App. 37a-39a.

The Commission further determined that its interpretation of "price," as used in the NGPA, was consistent with Congress's intent to establish a regulatory scheme that did not require review by the Commission of each individual natural gas sales contract. If the price of natural gas were adjusted to account for the value of the transportation of liquids and liquefiables "for every producer first sale the Commission would have the extraordinary difficult task of determining the value of the transportation service received by the producer to determine whether this amount, when

added to the monetary consideration, exceeds the applicable * * * maximum lawful price" (Pet. App. 42a). That result, the Commission found, would be directly contrary to Congress's attempt "to avoid uncertainty and delay by generally pricing gas at the wellhead in simple dollar amounts" (*id.* at 44a (footnote omitted)).

At the same time, the Commission made clear that the scope of its declaratory order was quite narrow. It observed that "unusual contractual arrangements could be structured solely for the purpose of evading the * * * price ceiling" and stated that such arrangements would be regulated under the Commission's enforcement authority (Pet. App. 41a n.21). In denying petitions for rehearing, the Commission reiterated that its order rested upon the fact that the "arrangements [regarding transportation of liquids and liquefiables] are a traditional part of pipeline-producer contracting practices" (*id.* at 62a). The Commission stated that it might reach a different result if presented with the question whether a non-traditional contract provision constituted a component of the price of natural gas.

2. The court of appeals unanimously affirmed the Commission's order (Pet. App. 24a-26a). The court observed that the Commission "has had a longstanding policy of requiring that the pipelines not allocate the[] costs [of providing transportation for liquids and liquefiables] to the consumer in their rate proceedings" (*id.* at 26a). Since the pipelines would be required to absorb these costs themselves, and could not pass along the costs to natural gas consumers, the court concluded that it was not "unreasonable or inconsistent with the purposes of the NGPA to require the pipelines to adhere to their contracts, provided adequate protection of the above-described policy is assured" (*ibid.*). The court determined that it was appropriate to "defer to the Commission's reading of the statute" because the court was "unpersuaded that the Congress

intended to require the Commission to consider this particular service as part of the price" of the natural gas (*ibid.*).[4]

## ARGUMENT

Petitioners misstate the scope of the Commission's order. Petitioners assert that the Commission declared that it "will, as a general rule, ignore non-monetary consideration" in determining whether a gas producer has received a price greater than the statutory maximum price (85-1207 Pet. 3), but in fact the Commission expressly limited the scope of its order to whether the price of natural gas must be adjusted to take account of free or below-cost transportation of liquids and liquefiables. In concluding that such an adjustment is not required, the Commission relied upon considerations specifically applicable only to that narrow question, including the need for efficiency in determining price and for consistency with prior and anticipated future regulatory practice. And the Commission cautioned that a different rule might apply with respect to other non-monetary consideration received by gas producers (Pet. App. 41a n.21, 62a). The decision of the court below affirming the Commission's narrow order is correct and does not conflict with any decision of this Court or another court of appeals. Further review by this Court is not warranted.

1. The Natural Gas Policy Act of 1978 (NGPA) "replace[d] the Commission's authority to fix rates of return to gas producers according to what is 'just and reasonable' with a precise schedule of price ceilings" applicable to "first sales" of certain types of natural gas. *Public Service Commission* v. *Mid-Louisiana Gas Co.*, 463 U.S. 319, 334

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[4]The court of appeals also affirmed in substantial part orders issued by the Commission relating to recovery by natural gas producers of production-related costs (Pet. App. 6a-24a) and concluded that another issue relating to recovery by pipelines of costs of transporting liquids and liquefiables was not yet ripe for review (*id.* at 27a-28a).

(1983); 15 U.S.C. 3331.[5] The statute prohibits sales of natural gas "at a first sale price in excess of any applicable maximum lawful price under [the NGPA]" (15 U.S.C. 3414(a)(1)). In order to determine whether a particular sale complied with these price ceilings, it is of course necessary to calculate the price at which the natural gas was sold. The question in this case is whether the price set forth in the express price term of a sales contract must be adjusted to account for any value received by the producer-seller as a result of the pipeline-purchaser's agreement to transport liquids and liquefiables owned by the producer-seller together with the natural gas purchased by the pipeline.

The NGPA does not prescribe the method for ascertaining the sales price of natural gas; indeed, the statute does not define the term "price." But Congress expressly authorized the Commission to administer the NGPA and "to define, by rule, accounting, technical, and trade terms" used in the NGPA (15 U.S.C. 3411(a) and (b)).[6] Since "the statute is silent * * * with respect to the specific issue" presented here, the question before this Court is whether the order issued by the Commission—the agency expressly charged with administering the statute—is "based on a permissible construction of the statute." *Chevron U.S.A. Inc.* v. *Natural Resources Defense Council,* 467 U.S. 837, 843 (1984) (footnote omitted). The Commission's determination must be "given controlling weight unless [it is] arbitrary, capricious, or manifestly contrary to the statute." *Id.* at 844 (footnote omitted);

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[5]A "first sale" is defined generally as a sale of natural gas to a pipeline company or a sale preceeding the sale of the gas to a pipeline company. 15 U.S.C. 3301(21).

[6]Although the Commission's action was denominated a declaratory order rather than a rule, the parties had the benefit of notice and an opportunity to comment. Petitioners have not raised in this Court any procedural challenge to the Commission's action.

see also *Chemical Manufacturers Ass'n* v. *Natural Resources Defense Council,* No. 83-1013 (Feb. 27, 1985), slip op. 8-9. The Commission's determination that the express contract price should not be adjusted in these circumstances, and that pipelines accordingly will not be relieved of contractual obligations to carry liquids and liquefiables at less than cost, plainly satisfies this standard of review.

a. As the Commission observed in its opinion (Pet. App. 35a-39a, 57a-59a), regulatory practice prior to the enactment of the NGPA is relevant in defining the price of a sale of natural gas because Congress enacted the NGPA "in the context of prevailing practices under the Natural Gas Act." Pet. App. 34a (footnote omitted); see also *Public Service Commission* v. *Mid-Louisiana Gas Co.,* 463 U.S. at 327-338 (interpreting NGPA by reference to prior regulatory scheme); *Process Gas Consumers Group* v. *United States Department of Agriculture,* 657 F.2d 459, 464-466 (D.C. Cir. 1981) (interpreting term in NGPA in accord with prior regulatory policy).

During the pre-NGPA period, in establishing "just and reasonable" rates for gas producers pursuant to its authority under the Natural Gas Act (see 15 U.S.C. 717c), the Commission typically did not consider the provision of free or below-cost transportation services to gas producers as a factor relevant to the producer's price for natural gas; the Commission's regulatory scheme generally did not provide for any adjustment to wellhead prices when a pipeline agreed to provide such transportation services. The Commission's policy "was, in almost all cases, to leave the consideration to be paid for the transportation and handling of [liquids and liquefiables] to private contractual negotiation between the parties" (Pet. App. 37a (footnote omitted)). And when reviewing pipeline rates under this same statutory authority, the Commission continued to distinguish between the amount paid by the pipeline for natural gas and

these transportation costs. The Commission determined the percentage of transportation costs attributable to the liquids and liquefiables and barred the pipeline from charging its natural gas customers for those costs. This practice ensured that natural gas customers would not be charged for transportation costs unrelated to natural gas. *Mobil Oil Corp.* v. *FPC*, 483 F.2d 1238, 1243 (D.C. Cir. 1973); Pet. App. 37a.[7]

The Commission's decision in the present case simply continues its prior regulatory approach. The transportation costs are considered separately from the natural gas price charged by the gas producers, and the Commission utilizes

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[7]Immediately prior to the enactment of the NGPA, the Commission used the basic approach of requiring the pipeline to ensure that the transportation costs were not allocated to natural gas customers. See *Tennessee Gas Pipeline Co.*, 38 F.P.C. 691, 698 (1967) (cost allocation a "firm Commission policy"); *High Island Offshore System*, 55 F.P.C. 2674, 2686, reh'g granted in part, 56 F.P.C. 725, 732 (1976). Petitioners thus are in error when they claim (85-1207 Pet. 6) that pipeline cost allocation did not exist prior to passage of the NGPA.

In the early days of producer wellhead rate setting, the Commission would sometimes adjust a producer's wellhead price downward to reflect the receipt of the transportation services. See *Continental Oil Co.*, 27 F.P.C. 96, 108 (1962). However, this producer rate adjustment—in essence the approach petitioners advocate here—ended with the initiation of the Commission's pre-NGPA area and nationwide producer rate regulations in the early 1970's.

For a short period in 1971 and 1972 the Commission pursued a third alternative, requiring pipelines to charge producers a specific rate for these transportation services. This approach first was implemented by settlement in one gas producing area. *Southern Louisiana Area*, 46 F.P.C. 86, 139 (1971), aff'd *sub nom. Placid Oil Co.* v. *FPC*, 483 F.2d 880 (5th Cir. 1973), aff'd *sub nom. Mobil Oil Corp.* v. *FPC*, 417 U.S. 283 (1974). The Commission subsequently attempted to impose this approach nationwide, but its rule was vacated on judicial review. See *Mobil Oil Corp.* v. *FPC*, 483 F.2d 1238 (D.C. Cir. 1973). Thus, petitioners again err in asserting (85-1207 Pet. 6 n.8) that this approach constituted the pre-NGPA regulatory practice; the approach in fact had been abandoned five years before enactment of the NGPA.

its regulatory authority under the Natural Gas Act to ensure that pipelines may not pass along to their natural gas customers any costs attributable to the transportation of liquids and liquefiables. Since these transportation costs were not considered part of the producers' price when those prices were regulated under the Natural Gas Act, there is no reason they should be included in the "price" under the NGPA regulatory scheme.

The Commission's decision also rests upon the relationship between the construction of "price" and the deregulation of natural gas prices (see 15 U.S.C. 3331). In a deregulated transaction, the rule urged by petitioners would impose upon natural gas customers what the Commission considered to be an unfair burden: pipelines would be permitted to pass along these transportation costs to their natural gas customers because the NGPA permits a pipeline to recover "any amount paid in any first sale of natural gas." See 15 U.S.C. 3431(b)(1)(A) and (c)(2). As the Commission observed (Pet. App. 68a (emphasis in original)), if the " 'amount paid' [for natural gas] includes the cost or value of liquids and liquefiables transportation service as petitioners allege, then *upon deregulation,* because the maximum lawful ceiling prices would cease to operate, this *entire* cost could automatically be passed through to gas customers of the pipeline, even though they may derive only a *partial* benefit from the transportation service, and even though the value or cost of the service may be *greater* than the cost of the gas." That result would conflict with the established principle that the Commission must "assure that users of gas are not asked to pay for the transportation of a commodity they are not using" (*Mobil Oil Corp.* v. *FPC*, 483 F.2d at 1249). There is no evidence that Congress intended

to abrogate this principle in enacting the NGPA. See Pet. App. 38a.[8]

b. The Commission's decision also accords with the basic statutory purpose of eliminating regulatory delay and uncertainty with respect to natural gas prices. In enacting the NGPA, Congress "explicitly establishe[d] an incentive pricing scheme that is wholly divorced from the traditional historical-cost methods applied by the Commission in implementing the [Natural Gas Act]" (*Public Service Commission* v. *Mid-Louisiana Gas Co.*, 463 U.S. at 333). This price structure was designed to promote production by reducing the regulatory burden generally; Congress particularly sought to eliminate gas producers' uncertainty about prices stemming from both regulatory delay and the Commission's emphasis upon historic costs. *Id.* at 331; H.R. Rep. 95-496, 95th Cong., 1st Sess. Pt. 4, at 96 (1977).

Petitioners' proposed interpretation of the NGPA would require the Commission to assign a dollar value to the transportation services for liquids and liquefiables provided under each individual natural gas purchase agreement (Pet. App. 42a-43a).[9] Even if the calculation of such a value were

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[8]Petitioners characterize (85-1190 Pet. 6-7) the Commission's decision as resting upon the conclusion that the statutory maximum prices may be disregarded because consumers will be protected under another statute. While this consumer protection certainly is important, petitioners have misapprehended the thrust of the Commission's decision. The Commission found that the past treatment of these costs, which was based on the goal of consumer protection, indicated that Congress could not have intended to include these costs within the definition of the price of natural gas.

Petitioners make essentially the same error in claiming (85-1190 Pet. 7-8) that the Commission's decision improperly increases the maximum prices established by statute. The decision simply gives content to the term price as it is used in the statute.

[9]This problem is exacerbated by the existence of two different methods for determining this value—calculating the actual cost to the

possible, the Commission would be required to engage in lengthy administrative proceedings to develop historic costs—the very practice that Congress sought to avoid in enacting the NGPA. As a result, uncertainty and regulatory delay would be reintroduced into natural gas pricing (Pet. App. 43a, 61a). The Commission correctly concluded (*id.* at 44a) that "[t]his massively complex system of costing and valuing every quantum of consideration was plainly not intended by Congress which generally sought in [the NGPA] to spur production by setting non-cost-based, incentive ceiling prices at the wellhead."[10]

Congress simply could not have intended to "require that the Commission assign a dollar value or cost to *all* the separate non-price aspects of the relationship between a gas producer and its buyer" (Pet. App. 43a (emphasis in original)), and the Commission therefore must be free to establish some limitation upon the definition of "price" for purposes of ascertaining compliance with the maximum price provisions of the NGPA. For the reasons discussed above,

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pipeline or assessing the benefit conferred upon the gas producers in view of the cost of alternative transportation methods. Pet. App. 33a-34a, 43a.

[10]Petitioners argue (85-1190 Pet. 5; 85-1207 Pet. 12) that the statutory definition of a "sale" as "any sale, exchange, or other transfer for value" (15 U.S.C. 3301(20)) is relevant in defining price. But the fact that a sale is defined as any "transfer for value" does not mean that "price" must be defined to include all non-monetary consideration.

Petitioners also contend (85-1207 Pet. 15) that the specific exclusion of state severance taxes and certain other costs from the calculation of the sales price (see 15 U.S.C. 3320) indicates that the Commission's order is erroneous. But nothing in the statute or the legislative history indicates that Section 3320 was intended to set forth an exclusive list of the items to be excluded in defining price, or that the provision otherwise limits the Commission's authority to define price.

the Commission, while reserving the right to take other non-monetary terms into account where circumstances warrant, correctly determined that the transportation services at issue here do not constitute an element of the price of natural gas within the meaning of the NGPA.

2. Petitioners challenge the Commission's determination on a variety of grounds, all of which are without merit. First, petitioners argue (85-1207 Pet. 11-12) that the term "price" ordinarily encompasses all consideration received by the seller under a sales contract. But while "consideration" includes all of the promises made by one contracting party to the other, the term "price" has a more limited meaning, referring to the value assigned to the subject of the contract and not including, for example, agreements with respect to transportation arrangements, insurance and risk of loss, warranties, and similar matters. Moreover, the Commission properly interpreted this statutory term by reference to prior regulatory practice and Congress's purposes in enacting the NGPA (see pages 8-12, *supra*). Finally, Congress specifically authorized the Commission to administer the statute; because the Commission's definition is not "arbitrary, capricious, or manifestly contrary to the statute" it should be given "controlling weight" (*Chevron U.S.A. Inc.* v. *Natural Resources Defense Council,* 467 U.S. at 844 (footnote omitted)).

Second, petitioners argue (85-1207 Pet. 16-18) that the Commission's definition of price improperly preempts state law. Petitioners did not present this argument to the Commission or the court of appeals and therefore may not raise it before this Court. *United States* v. *Lovasco,* 431 U.S. 783, 788 n.7 (1977); *Adickes* v. *S.H. Kress & Co.,* 398 U.S. 144, 147 n.2 (1970); see also *Ecee, Inc.* v. *FERC,* 611 F.2d 554, 559-566 (5th Cir. 1980). Moreover, the argument is based entirely on the spurious assumption that Congress intended "price" to be defined by reference to state law, and

there is no evidence that Congress so intended. The argument also assumes that the Commission's construction of the statute somehow will interfere with state law. However, the Commission's order simply applies federal law to define a term in a federal statute; it does not in any way alter the state law rules of construction otherwise applicable to natural gas sales contracts. There simply is no preemption issue in this case.[11]

Third, petitioners argue (85-1190 Pet. 6; 85-1207 Pet. 7) that the Commission's order permits gas producers to avoid the maximum prices established in the NGPA, but this is only another way of asserting that the Commission erred in defining "price." The Commission's decision was extremely narrow, applying only to the specific transportation costs that had been excluded from the definition of price under prior regulatory practice, and the effect of the Commission's decision is only to avoid relieving pipelines of what may have been improvident promises to provide transportation services whose cost the pipeline companies must absorb and may not pass on to their natural gas customers. Petitioners' attempt to elevate the Commission's narrow decision (see Pet. App. 41a n.21, 62a) into a broad determination to ignore all non-monetary consideration is wholly without merit.[12]

In the final analysis, the Commission's order simply represents a continuation of past regulatory policy, not a novel administrative development. It is consistent with the

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[11]Petitioners similarly argue (85-1207 Pet. 13-14) that the Commission's order interferes with the contractual rights of the parties to these contracts. However, the order permits buyers and sellers to enter into any contract permissible under the NGPA.

[12]Indeed, petitioners themselves cite (85-1207 Pet. 10 n.18) several documents indicating that other sorts of non-monetary consideration might be considered to be components of the price of natural gas.

existing practices in the industry, Congress's intent in enacting the NGPA, and common sense. The court of appeals therefore correctly upheld the Commission's order.

## CONCLUSION

The petitions for a writ of certiorari should be denied.

Respectfully submitted.

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IN THE

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ASSOCIATED GAS DISTRIBUTORS AND PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, PETITIONERS

v.

FEDERAL ENERGY REGULATORY COMMISSION

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TRANSCONTINENTAL GAS PIPE LINE CORP., ET AL., PETITIONERS

v.

FEDERAL ENERGY REGULATORY COMMISSION

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**On Petitions for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit**

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## REPLY BRIEF OF PETITIONERS ASSOCIATED GAS DISTRIBUTORS AND PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK

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## REPLY BRIEF OF PETITIONERS ASSOCIATED GAS DISTRIBUTORS AND PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK

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Pursuant to Rule 22.5 of this Court, Petitioners, Associated Gas Distributors and the Public Service Commission of the State of New York, hereby reply to the briefs in opposition to their petition filed by Respondent Federal Energy Regulatory Commission (Commission) and the "undersigned producers" (Producers). The briefs in opposition fail to justify the decision of the court below, which erroneously affirmed the Commission's holding that natural gas producers may receive both the maximum lawful price allowed under the Natural Gas Policy Act of 1978, 15 U.S.C. § 3301 *et seq.*, (NGPA), in cash *and* additional value in the form of free or underpriced transportation of producer-owned liquids and liquefiables, without violating Section 504(a) of the NGPA, which prohibits the sale of "natural gas at a first sale price in excess of any applicable maximum lawful price". 15 U.S.C. § 3414(a).

The Commission argues that the decision of the court below can be affirmed because the Commission's decision: (1) was consistent with its treatment of liquids and liquefiables transportation for purposes of producer and pipeline rate regulation prior to the NGPA, (2) was a proper exercise of its authority to define terms used in the NGPA, and (3) avoids the administrative burden and regulatory delay involved in determining the value of non-monetary consideration received by producers. For the reasons stated below, the Commission's arugments should be rejected.

1. The Commission's treatment of liquids and liquefiables transportation for purposes of producer or pipeline rate regulation under the Natural Gas Act of 1938, 15 U.S.C. §§ 717 et seq. (NGA), has no bearing whatsoever on whether the ceiling price provisions of the NGPA have been violated. As the Court stated in *Public Service Commission v. Mid-Louisiana Gas Co.*, 463 U.S. 319, 322 (1983), the NGPA: (1) "comprehensively and dramatically changed the method of pricing natural gas produced in the United States", (2) "explicitly estab-

lishes an incentive pricing scheme that is wholly divorced from the traditional historical-cost methods applied by the Commission in implementing the NGA", *Id.* at 333, and (3) "replaces the Commission's authority to fix rates of return to gas producers according to what is 'just and reasonable' with a precise schedule of price ceilings", *Id.* at 334. The Commission's authority to adjust the NGPA price ceilings is strictly limited.[1] None of the exceptions to the ceiling price limitations expressly permitted by Congress in Title I of the NGPA applies to the additional value at issue here. Receipt of these valuable services in addition to the maximum lawful price in cash, therefore, constitutes a violation of the first sale price limitations in Section 504(a)(1) of the NGPA. Petition in No. 85-1190 at 7-8. The Commission's rate regulation practice under the NGA is irrelevant to the issue before the Court here.

2. The Commission's authority under NGPA Section 501(b) to define terms used in the NGPA must be exercised in a manner "consistent with the definitions set forth" in the Act. 15 U.S.C. § 3411(b). In this case, the Commission has abused its authority under Section 501(b) by ignoring the definition of the term "sale" in NGPA Section 2(20), 15 U.S.C. § 3301(20), ("any sale, exchange, or other transfer for value") in interpreting the critical term "first sale price" in Section 504(a)(1), 15 U.S.C. Section 3414(a)(1). See Petition in No. 85-1190 at 5.

3. The Commission's argument that determining the value of liquids and liquefiables transportation services would entail lengthy administrative proceedings with a resulting delay and uncertainty with respect to natural gas prices should be rejected. The Commission must do

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[1] See NGPA Sections 104(b)(2), 106(c), 107(b), 109(b)(2), and 110, 15 U.S.C. §§ 3314(b)(2), 3316(c), 3317(b), 3319(b)(2) and 3320.

whatever is necessary to prevent violations of the NGPA. In this case, the Commission has refused to even initiate a proceeding to determine the value of liquids and liquefiables transportation in relation to NGPA ceiling price limitations. Its protests about administrative burden and delay are merely speculative and self-serving.

4. The Producers' brief in opposition attempts to defend the orders of the Commission and the Court below by distinguishing the price paid for natural gas produced at the wellhead from the consideration for services performed after the gas leaves the wellhead. Producers' Brief at 5-9. Neither the Commission nor the court below rested its decision on any such distinction. The Producers' argument simply misses the mark.

5. In sum, neither the Commission's nor the Producers' brief in opposition to the petition for certiorari comes to grips with the fundamental error before the Court in this case: a violation of the ceiling price provisions of Title I of the NGPA cannot be excused on the basis of the Commission's rate regulation practices under the NGA or on the basis that pipeline customers may be protected from paying the pipelines' costs of providing liquids and liquefiables services to the producers in rate proceedings under the NGA. The NGPA makes it unlawful for producers to receive a first sale price in excess of the Title I ceiling prices. The Commission's Declaratory Order and the order of the court below affirming it are in conflict with the clear language of the NGPA, invite circumvention of the NGPA ceiling price limitations, and would permit substantial windfall profits not intended by Congress.

## CONCLUSION

For the foregoing reasons, Petitioners request that their petition for a writ of certiorari be granted.

Respectfully submitted,

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*Respondent.*

TRANSCONTINENTAL GAS PIPE LINE
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*Respondent.*

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## REPLY BRIEF OF TRANSCONTINENTAL GAS PIPE LINE CORPORATION, ET AL.

---

Pursuant to Rule 22.5 of this Court, Transcontinental Gas Pipe Line Corporation, *et al.*, ("Petitioners") hereby reply to the Briefs in Opposition to the Petition for Writ of Certiorari in the above-captioned cases that were filed by the Federal Energy Regulatory Commission ("FERC") and certain producer intervenors ("Produc-

ers") on April 23, 1986. In their briefs in opposition, the FERC and the Producers each contend that Petitioners have mischaracterized the rationale underpinning the Declaratory Order here in issue (Pet. App. B, at 29a-50a) but even these parties disagree as to the basis for the Order.[1] Each party also contends that the Order is a proper interpretation of the Natural Gas Policy Act of 1978 ("NGPA"),[2] principally because it allegedly continues pre-NGPA regulatory practice.

1. Significantly, the FERC and the Producers do not dispute the importance of the issue decided in the Order. Even the court below recognized the importance of the issue, stating that the Order raised "the specter of opening a gaping loophole in the maximum lawful price provisions in the NGPA." (Pet. App. A, at 26a). The specter recognized by the court below is very real. Essentially, the Order is based on the FERC's perception that it is authorized to pick and choose among those elements of valuable consideration set forth in a contract that it will consider when applying Congressionally-established maximum lawful price ceilings. While the Order addresses only one type of consideration received by producers—*i.e.*, free or partially unreimbursed liquids and liquefiable transportation service—the principle involved could be equally applicable to *any* type of consideration provided for in gas purchase contracts. Thus, this case presents the fundamental and important ques-

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1. The FERC argues that the basis of the Order is to remove price uncertainty and avoid administrative difficulty. (FERC Br., at 6). On the other hand, the Producers argue that the basis of the Order is a distinction between the price of gas at the wellhead and consideration for services rendered beyond the wellhead. (Prod. Br., at 5-6).

2. 15 U.S.C. §§ 3301-3432 (Supp. 1985).

tion of how Congress intended its ceiling price structure to be enforced.[3]

2. The cornerstone of the FERC's and the producers' defense of the Order, and the principal basis for the rationale of the court below, is a cost allocation policy adopted by the FERC in pipeline rate cases which requires that pipelines absorb certain transportation costs not fully reimbursed by producer suppliers. That cost allocation policy[4] is totally irrelevant for purposes of ascertaining Congress' intent regarding the applicability of maximum lawful price ceilings because it has no bearing whatsoever on the price collected by producers under their contracts for the first sale of natural gas. Since Congressional ceiling price limitations apply only to the prices received by producers, the only pertinent question is whether admittedly valuable consideration in the form of free or discounted transportation services received by producers is part of the "first sale price" subject to Congressionally-established price ceilings. A cost allocation policy *used only in pipeline ratemaking* has no bearing on the relevant question and Congress would

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3. In Public Service Commission v. Mid-Louisiana Gas Company, 463 U.S. 319, 334 (1983), this Court held that the NGPA established a "precise schedule of price ceilings." The question of whether those precise ceiling prices are properly enforced in terms of only part, but not all, of the "first sale price" subject to regulation represents a question that will reoccur with respect to other types of non-monetary consideration set forth in gas purchase contracts.

4. FERC claims that its pipeline cost allocation policy predated enactment of the NGPA, which is inaccurate. That dispute is academic, however, because the policy has no bearing on producer prices. Significantly, the Commission can cite no case where a producer was affirmatively permitted to collect NGA ceiling prices as well as additional consideration in the form of free or partially unreimbursed transportation service.

not have relied on that policy in developing maximum lawful ceiling prices applicable to first sales of gas.

3. The FERC and the Producers argue that the Commission can adopt any reasonable interpretation of the meaning of "first sale price" because Congress was silent on its intent. However, Congress was *not* silent on the question of what constituted the "first sale price" subject to the regulatory ceiling prices established in Title I. Section 101(b)(9) of the NGPA[5] makes it clear that the "first sale price" was intended to be the contract price. Petitioners submit that it is totally unreasonable for the FERC to substitute its own notions of what constitutes "price" where Congress expressly indicated that the contract should control. By indicating that the contract would control the determination of the "first sale price" for gas, the only reasonable conclusion is that Congress intended that disputes with respect to what constitutes the "price" would be resolved in accordance with general principles of contract law, where price is all of the consideration received by a seller.[6] However, instead of relying on the generally accepted concepts of price in contract law, the Order announced a federal rule totally at odds with contract law principles. While the FERC attempts to justify this federal rule as providing for certainty in gas pricing and efficiency in administration, those justifications ignore the overriding question of whether *Congress* intended new rules of contract con-

5. 15 U.S.C. § 3311(b)(9).

6. Indeed, in Pennzoil Company v. Federal Energy Regulatory Commission, 645 F.2d 350 (5th Cir. 1981), *cert. denied*, 454 U.S. 1142 (1982), the court expressly held that FERC use state rules of contract construction when determining the price allowed by gas purchase contracts.

struction to be imposed on pre-existing private contracts.[7]

4. The FERC and the Producers also argue that Congress could not have intended the agency to assign a value to every aspect of non-monetary consideration contained in gas purchase contracts when enforcing the NGPA's price ceilings.[8] This argument ignores the fact that this Court long ago admonished the FERC's predecessor agency to consider the value of unreimbursed transportation services when regulating producer rates pursuant to the Natural Gas Act ("NGA"), 15 U.S.C. §§ 717, *et seq.* (Supp. 1985).[9] There is absolutely no indication in the NGPA that Congress intended the NGPA's maximum lawful ceiling prices to be less comprehensive than the regulation previously applicable under the NGA. Section 504(a) of the NGPA,[10] states that it "shall be unlawful for any person . . . to sell natural gas at a first sale price in excess of any applicable maximum

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7. The FERC erroneously claims that Petitioners did not preserve this issue by presenting it below. As the FERC itself recognized, several rehearing petitions "couch the Title I question as involving contract law only." (Pet. App. C, at 56a). Obviously, the question of whether FERC was bound by general contract principles when interpreting a contract was preserved for review.

8. In Section 110 of the NGPA Congress expressly allowed recovery of production-related costs in addition to maximum lawful ceiling prices. The FERC undertook the complicated task of assigning values to production-related services where the producers would benefit. If Congress did not view administrative difficulty as bar to the FERC action in regard to additional compensation for producers, it would be equally true that Congress did not intend that administrative difficulty be invoked where the enforcement of price ceilings was at issue.

9. *Atlantic Refining Company v. Public Service Commission*, 360 U.S. 378 (1959).

10. 15 U.S.C. § 3414(a).

lawful price under this Act." This language gives no indication that an unlawful price may be forgiven, even if it is administratively difficult to determine the value to be assigned to non-monetary consideration.

Given the importance of the question presented and the significance of the resolution of this question to administration of the NGPA, the writ should be granted.

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